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IN THE

Supreme Court of the United States

OCTOBER TERM, 1997

NATIONSMART CORPORATION, ET AL.,
Petitioners,

v.

HELEN S. PALMQUIST, BRIAN PALMQUIST, JOHN D. PALMQUIST, AND JACK CARLON,
Respondents.

Petition for a Writ of Certiorari to the
United States Court of Appeals for the Eighth Circuit

PETITION FOR WRIT OF CERTIORARI

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QUESTIONS PRESENTED FOR REVIEW

I

Whether the phrase "averments of fraud" in Rule 9(b) of the Federal Rules of Civil Procedure encompasses averments of fraud where scienter is not a required element of a plaintiff's cause of action.

II

Whether the phrase "averments of fraud" in Rule 9(b) of the Federal Rules of Civil Procedure encompasses averments that representations were made without a reasonable basis.

III

Whether risk disclosures that are tailored to a company's projections must predict the precise timing of future business reverses in order to render the projections immaterial under the federal securities laws.

LIST OF PARTIES, PARENT CORPORATIONS, AND SUBSIDIARIES

Petitioners:

NationsMart Corporation,
PCIA, Inc. (formerly Pauli & Company, Inc.),
RAS Securities Corp.,
S. Leslie Flegel,
Alan G. Johnson,
Franklin A. Jacobs,
S. Lee Kling,
Michael J. Dunlap,
Alice E. Brueggemann, and
Michael E. Thaman.

Appellee Below (now deceased):

Mel A. Friedman.

Respondents:

Helen S. Palmquist,
Brian Palmquist,
John D. Palmquist, and
Jack Carlon;
individually and on behalf of others similarly situated.

The parent corporation of NationsMart Corporation is RAS Securities Corp. NationsMart Corporation has no subsidiaries other than wholly owned subsidiaries. There is no parent company of PCIA, Inc. PCIA, Inc. has no subsidiaries other than wholly owned subsidiaries. There is no parent company of RAS Securities Corp. The only subsidiary of RAS Securities Corp., other than wholly owned subsidiaries, is NationsMart Corporation.

TABLE OF CONTENTS

	Page
Questions Presented for Review	i
List of Parties, Parent Corporations, and Subsidiaries	ii
Table of Authorities	v
Opinions Below	1
Jurisdiction	1
Statutes and Regulations Involved	2
Statement of the Case	2
A. NationsMart's Initial Public Offering	2
B. Course of Proceedings and Disposition Below	4
Reasons for Granting the Writ	6
I. This Court Should Resolve the Split Among the Circuits Concerningthe Meaning and Applicability of Rule 9(b)	6
A. The Circuits Are Split on the Applicability of Rule 9(b) to Averments of Fraud in Support of Causes of Action for Which Scienter is Not a Required Element	6
B. The Eighth Circuit's Opinion Abrogates an Entire Category of Fraud From the Reach of Rule 9(b)	11
II. The Eighth Circuit's Interpretation of the Bespeaks Caution Doctrine Eviscerates the Doctrine and Directly Conflicts with Decisions of Other Circuits	12

Conclusion 16

Appendix

A Opinion of the Court of Appeals dated November 21, 1997 ..... A-1

B Opinion of the District Court dated April 11, 1996. B-1

C Opinion of the District Court dated November 6, 1996 ..... C-1

D Opinion of the District Court dated December 2, 1996 ..... D-1

E Order of the Court of Appeals Denying Rehearing dated January 15, 1998 ..... E-1

F Statutes and Regulations F-1

TABLE OF AUTHORITIES

Cases	Page(s)
Arazie v. Mullane, 2 F.3d 1456 (7th Cir. 1993)	8
Basic, Inc. v. Levinson, 485 U.S. 224 (1988)	12
Blue Chip Stamps, 421 U.S. 723 (1975)	15
Collins v. Burns, 103 Nev. 394, 741 P.2d 819 (1987)	11
In re Consumers Power Co., Sec. Litig., 105 F.R.D. 583 (E.D. Mich. 1985)	9
In re Donald J. Trump Casino Sec. Litig., 7 F.3d 357 (3d Cir. 1993), *cert. denied*, 510 U.S. 1178 (1994)	13
Gasner v. Board of Supervisors, 103 F.3d 351 (4th Cir. 1996)	14
Gold v. Morrison-Knudsen Co., 68 F.3d 1475 (2d Cir. 1995) *cert. denied*, 517 U.S. 1213 (1996)	7
Leatherman v. Tarrant Co. Narcotics Intelligence and Coordination Unit, 507 U.S. 163 (1993)	9
Melder v. Morris, 27 F.3d 1097 (5th Cir. 1994)	7
Nielsen v. Adams, 223 Neb. 262, 388 N.W.2d 840 (1986)	11
Pavelic & LeFlore v. Marvel Entertainment Group, 493 U.S. 120 (1989)	8
Schwartz v. Celestial Seasonings, Inc., 124 F.3d 1246 (10th Cir. 1997)	7
Sears v. Likens, 912 F.2d 889 (7th Cir. 1990)	7
Shapiro v. UJB Fin. Corp., 964 F.2d 272 (3d Cir.), *cert. denied*, 506 U.S. 934 (1992)	7

Shaw v. Digital Equip. Corp., 82 F.3d 1194 (1st Cir. 1996) 7

In re Stac Electronics Sec. Litig., 89 F.3d 1399 (9th Cir. 1996), *cert. denied*, 117 S. Ct. 1105 (1997) 7,8,10

Suna v. Bailey Corp., 107 F.3d 64 (1st Cir. 1997) 14

TSC Indus., Inc. v. Northway, Inc., 426 U.S. 438 (1976) 12,13

Virginia Bankshares, Inc. v. Sandberg, 501 U.S. 1083 (1991) 12

In re Worlds of Wonder Sec. Litig., 35 F.3d 1407 (9th Cir. 1994), *cert. denied*, 516 U.S. 909 (1995) 13

Statutes and Regulations

15 U.S.C. §77k (1994) 4

15 U.S.C. §77*l*(2) (1994) 4

15 U.S.C. §77v (1994) 4,15

15 U.S.C. §78a (1994) 4

15 U.S.C. §78j(b) (1994) 4

15 U.S.C. §78u-4(b) (1994) (Supp. I 1995) 10

15 U.S.C. §77z-1 (1994) (Supp. I 1995) 10

15 U.S.C. §78aa (1994) 15

17 C.F.R. §229.303 (1997) 15

17 C.F.R. §229.10(b) (1997) 15

17 C.F.R. §230.175 (1997) 5,11

28 U.S.C. §1254(1) (1994) 1

28 U.S.C. §1331 (1994) 4

FED. R. CIV. P., Rule 8(a) 8

FED. R. CIV. P., Rule 9 2,5-12

FED. R. CIV. P., Rule 10(b) 8

FED. R. CIV. P., Rule 12(b)(6) 5

PETITION FOR WRIT OF CERTIORARI

Petitioners NationsMart Corporation, PCIA, Inc., RAS Securities Corp., S. Leslie Flegel, S. Lee Kling, Franklin A. Jacobs, Alan G. Johnson, Michael J. Dunlap, Alice E. Brueggemann, and Michael E. Thaman respectfully petition for a writ of certiorari to review the judgment of the United States Court of Appeals for the Eighth Circuit in this case.

OPINIONS BELOW

The opinion of the court of appeals is reported at 130 F.3d 309 (8th Cir. 1997). It is reprinted in the Appendix as Appendix A. The district court's unpublished opinion and order of April 11, 1996 is reprinted as Appendix B. The district court's unpublished opinion and order of November 6, 1996 is reprinted as Appendix C. The district court's unpublished opinion and order of December 2, 1996 is reprinted as Appendix D. The court of appeals' order denying Petitioners' petition for rehearing and suggestion for rehearing en banc is not reported and is reprinted at Appendix E.

JURISDICTION

The court of appeals entered its judgment on November 21, 1997. It denied a timely petition for rehearing and suggestion for rehearing en banc on January 15, 1998. This Court has jurisdiction to review the judgment by writ of certiorari under 28 U.S.C. §1254(1).

STATUTES AND REGULATIONS INVOLVED

Federal Rules of Civil Procedure, Rule 9(b):

Rule 9. Pleading Special Matters

. . . .

> **(b) Fraud, Mistake, Condition of the Mind.** In all averments of fraud or mistake, the circumstances constituting fraud or mistake shall be stated with particularity. Malice, intent, knowledge, and other condition of mind of a person may be averred generally.

STATEMENT OF THE CASE

This securities fraud class action involves an initial public offering of the stock of NationsMart Corporation ("NationsMart") in December 1993. NationsMart was founded in 1992 by private investors who hoped to capitalize on the retail "supercenter" concept by placing dry-cleaning, laundry, and shoe repair centers in the vestibules of large Wal-Mart and Kmart stores. (A 2.) By the end of 1993, NationsMart had opened a total of 51 centers. (A 3.) In December 1993, NationsMart filed a Registration Statement and Prospectus with the Securities and Exchange Commission ("SEC") and commenced an initial public offering of securities that was intended to raise $11.7 million in capital. (A 2-3.)

A. NationsMart's Initial Public Offering

The predictions and warnings contained in the Prospectus are undisputed. The Prospectus disclosed NationsMart's goal of opening 600 new centers within five years and management's belief that the proceeds of the offering would be sufficient to open 108 stores and to operate existing stores through October 1994. (A 3.) These predictions were presented in the context of a series of cautions, including the warning that the company had

"recurring operating losses and limited capital resources" and that its accountants reported that "substantial doubt exists as to the Company's ability to continue as a going concern." (A 3; B 7.) NationsMart explained that it "expects to continue to incur net losses and negative cash flow from operations during 1994 and 1995" (A 13), and that "[t]here can be no assurance that any of the Company's Centers or that the Company as a whole will generate income from operations or provide cash from operating activities in the future." (A 13.) The Prospectus further warned investors that the proceeds of the offering would not be sufficient to underwrite its business plan and that, in ten months, it "will require capital resources in addition to those provided by the proceeds of this offering" to keep operating, and that "[t]he Company has no definitive arrangements to obtain additional funding." (A 12; B 9.) The company also advised potential investors that the offering would not be sufficient to "provide funds for unforeseen general corporate purposes" (B 9) and that "[s]uccessful implementation of [the Company's] business plan is subject to a variety of risks associated with rapid growth, including the Company's ability to attract and retain qualified personnel, integrate new Centers into the Company's operations and the availability of adequate external sources of financing." (A 3; B 9.)

After the offering, NationsMart spent more money to open centers than expected, opened fewer centers than anticipated, and experienced significant turnover in management. (A 3-4; B 11, 13-14.) NationsMart replaced its Chief Financial Officer in March 1994. (A 4; B 11.) In June 1994, NationsMart replaced its Chief Executive Officer, and then lost the new CEO in an automobile accident three months later. (B 13; Amended Complaint ¶ 52.) NationsMart's stock price gradually declined from the offering price of $7.00 per share in December 1993 to $1.25 per share by October 1994. (A 4; B 14.) The stock continued to decline in value until it was delisted in mid-1995. (A 4.)

B. Course of Proceedings and Disposition Below

Plaintiffs (Respondents here) filed this action in November 1994, and in May 1995, they filed a Consolidated Amended Class Action Complaint (the "Amended Complaint"). (A4.) The Amended Complaint alleged a single fraudulent scheme as the purported basis of liability under Sections 11 and 12(2) of the Securities Act of 1933 (the "1933 Act"), 15 U.S.C. §§77k and 77*l*(2),[1] and Section 10(b) of the Securities Exchange Act of 1934 (the "1934 Act"), 15 U.S.C. §78j(b). The Amended Complaint alleged jurisdiction in the federal district court under 28 U.S.C. §1331 and 15 U.S.C. §§77v and 78a.

Plaintiffs alleged that defendants knew that the projections in the Prospectus were false, misleading, and/or without reasonable basis, and that they intended the Prospectus to mislead investors.[2] These fraud allegations were incorporated by reference into each of the three counts of the Amended Complaint and formed the only factual bases for the 1933 Act claims. (C4; Amended Complaint ¶¶66, 75.) At the end of each claim, plaintiffs inserted the following disclaimer:

> Plaintiffs do not allege in this [] claim that defendants, or any of them, were guilty of scienter, that is, of any scheme to defraud or of any misrepresentations or omissions that were made intentionally or recklessly.

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[1] After this case was filed, these statutory provisions were amended in part (not relevant here) by the Private Securities Litigation Reform Act of 1995, P.L. 104-67, Tit. I, §105, 109 Stat. 757 (1995) (the "Reform Act"), and §77*l*(2) was renumbered as §77*l*(a)(2).

[2] *See, e.g.*, C 5 n.2; Amended Complaint ¶2 ("[D]efendants concealed the adverse developments .. [and] made a series of misleading disclosures, which were designed to and did conceal NationsMart's problems from the market."), ¶31 ("The defendants knew that the projections they intended to release to the investing public ... were false and had no reasonable basis [.]"); *see also* Amended Complaint ¶¶16(b), 22, 30, 37, 64, 65.

(C 6 n.3; Amended Complaint ¶¶74, 80; A 7.) The Amended Complaint contained no allegations of negligence or innocent misrepresentation.

In April 1996, the district court dismissed nearly the entire Amended Complaint. The claims based on predictive statements in the Prospectus were dismissed under both FED. R. CIV. P. 12(b)(6) for failure to plead a material misstatement pursuant to the bespeaks caution doctrine and under FED. R. CIV. P. 9(b) ("Rule 9(b)") for failure to plead with particularity the circumstances of the alleged fraud. (A 5.)[3] The Court of Appeals for the Eighth Circuit affirmed the district court's dismissal of the 1934 Act claim, but reversed the dismissal of the 1933 Act claims, which were based on the same factual allegations. (A 6, 14, 17.)

The Eighth Circuit held that 1933 Act claims need never be alleged with particularity -- regardless of a plaintiff's factual averments "because proof of fraud and scienter are not necessary for recovery" under the 1933 Act. (A15; *see also* A 6, 8.) The court also held that a plaintiff's one-sentence disclaimer is sufficient to nullify factual averments of fraud for purposes of Rule 9(b). (A 7.) The court further held that "fraud" for purposes of Rule 9(b) does not include forward-looking statements made without any reasonable basis.[4] (A9-11.) The Eighth Circuit also found that the warnings in the prospectus did not render the projections immaterial under the bespeaks caution doctrine because the Company had not predicted *precisely when* it would run out of money. (A 13.) Judge Beam dissented from this holding, noting:

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[3] The district court resolved the few remaining issues in the case, not at issue here, in November 1996. (A 16 n.5.)

[4] SEC Rule 175, 17 C.F.R. §230.175, provides that plaintiffs who challenge forward-looking statements under the 1933 Act must "show[] that such statement was made or reaffirmed without a reasonable basis or was disclosed other than in good faith." (*See* A 9; F 8.)

> It is difficult for me to envision how or in what manner, defendants could have advanced greater warnings to potential investors so as to avail themselves of the "bespeaks caution" doctrine.

(A 24.)

REASONS FOR GRANTING THE WRIT

The Court should grant a writ of certiorari in this case in order to resolve circuit splits on two important issues: the proper reach of Rule 9(b) of the Federal Rules of Civil Procedure, and the proper standard for evaluating the materiality of a prediction under the federal securities laws.

I. THIS COURT SHOULD RESOLVE THE SPLIT AMONG THE CIRCUITS CONCERNING THE MEANING AND APPLICABILITY OF RULE 9(b).

The Eighth Circuit's decision directly conflicts with decisions in other circuits concerning the meaning of the phrase "averments of fraud" in Rule 9(b) of the Federal Rules of Civil Procedure.[5] The Eighth Circuit interpreted the term "averments" to refer not to allegations of fraud but rather to claims requiring proof of fraud. Moreover, the Eighth Circuit excluded statements made without a reasonable basis from the definition of "fraud" for purposes of Rule 9(b).

A. The Circuits Are Split On The Applicability Of Rule 9(b) To Averments Of Fraud In Support Of Causes of Action For Which Scienter Is Not A Required Element.

The Eighth Circuit's decision that Rule 9(b) of the Federal Rules of Civil Procedure can never apply to claims under

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[5] Rule 9(b) provides that, "[i]n all averments of fraud or mistake, the circumstances constituting fraud or mistake shall be stated with particularity."

Sections 11 and 12(2) of the Securities Act of 1933 (the "1933 Act claims") directly conflicts with decisions in the First, Third, Fifth, and Ninth Circuits. *See Shaw v. Digital Equip. Corp.*, 82 F.3d 1194, 1223 (1st Cir. 1996); *Shapiro v. UJB Fin. Corp.*, 964 F.2d 272, 287-88 (3d Cir.), *cert. denied*, 506 U.S. 934 (1992); *Melder v. Morris*, 27 F.3d 1097, 1100 n.6 (5th Cir. 1994); *In re Stac Electronics Sec. Litig.*, 89 F.3d 1399, 1404-05 (9th Cir. 1996), *cert. denied*, 117 S.Ct. 1105 (1997).[6] The courts in these cases analyzed the question of whether the particularity requirements of Rule 9(b) should apply by looking beyond the formal elements of the claim to "examine the factual allegations that support a particular legal claim." *Shapiro*, 964 F.2d at 288. Where the gravamen of the averments is fraud, these circuits hold that Rule 9(b)'s particularity requirements must be satisfied, regardless of whether fraud is a required element of the cause of action. *See Shaw*, 82 F.3d at 1223 ("The threshold question is whether the Wilensky complaint . . . contains 'averments of fraud.'"); *Shapiro*, 964 F.2d at 288 ("Rule 9(b) refers to 'averments' of fraud, and thus requires us to examine the factual allegations that support a particular legal claim."); *Melder*, 27 F.3d at 1100 n.6 ("When 1933 Securities Act claims are grounded in fraud rather than negligence . . . Rule 9(b) applies."); *Stac*, 89F.3d at 1405 ("Because [Rule 9(b)'s] policy considerations apply to Section 11 claims sounding in fraud, we hold that persons making such claims must state with particularity the circumstances constituting the alleged fraud."); *see also Gold v. Morrison-Knudsen Co.*, 68 F.3d 1475, 1477 (2d Cir. 1995) (applying Rule 9(b) to False Claims Act pleading despite a "liberal scienter requirement"), *cert. denied*, 517 U.S. 1213 (1996).

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[6] *See also Sears v. Likens*, 912 F.2d 889, 892-93 (7th Cir. 1990) (applying Rule 9(b) to fraud allegations under 1933 Act without discussion); *Schwartz v. Celestial Seasonings, Inc.*, 124 F.3d 1246, 1252 (10th Cir. 1997) ("assuming without deciding" that Rule 9(b) applies to Section 11 claims alleging fraud).

This analysis comports with the language of Rule 9(b), which by its terms applies to "averments of fraud" and not merely to claims in which fraud is an element. *See Pavelic & LeFlore v. Marvel Entertainment Group*, 493 U.S. 120, 123 (1989) (holding that analysis of FED. R. CIV. PROC. 11 begins with plain language of rule). Rule 9(b) states:

> In all averments of fraud or mistake, the circumstances constituting fraud or mistake shall be stated with particularity. Malice, intent, knowledge, and other condition of mind of a person may be averred generally.

The Federal Rules of Civil Procedure draw a clear distinction between "averments" and "claims." "Averments" are individual allegations in numbered paragraphs; "claims" are causes of action containing multiple averments. FED. R. CIV. P. 10(b); *see also* FED. R. CIV. P. 8(a) (enumerating the various averments required for each claim). Under the Federal Rules, the term "averments" does not mean "claims for relief." Thus, by its terms, Rule 9(b) applies to individual allegations of fraud and not merely to causes of action in which fraud is an essential element.

The analysis of the First, Third, Fifth, and Ninth Circuits is also consistent with the primary purposes of Rule 9(b): to protect the defendant's reputation from unsupported attacks on his or her integrity, and "to protect companies that have suffered business reverses from strike suits brought by disgruntled investors." FED. R. CIV. P. 9 (Advisory Committee Notes); *Arazie v. Mullane*, 2 F.3d 1456, 1465 (7th Cir. 1993); *Stac*, 89 F.3d at 1405. A charge of fraud is a serious one, and a generalized averment of fraud is both easily made and virtually impossible to defend against. A particularized averment of fraud, however, may be challenged or disproven. Rule 9(b) evens the playing field so that a defendant has a fair chance to defend against the serious and stigmatizing charge of fraud.

The Eighth Circuit's holding that the particularity requirements of Rule 9(b) can never apply to averments of fraud within 1933 Act claims "because proof of fraud and scienter are not necessary for recovery" (A 15) is in direct conflict with decisions of its sister circuits, the plain language of Rule 9(b), and the purposes of the rule.[7] The Eighth Circuit ignored the plain language of Rule 9(b), which requires particularity in "all averments of fraud." and instead rephrased the rule as applying to "a complaint averring fraud." (A 6.) As a result, the Eighth Circuit held that Rule 9(b) applies only to claims in which fraud is a required element and therefore provides no protection from strike suits or unsupported attacks on defendants' reputations.[8] Further, the Eighth Circuit's ruling requires courts to treat identical averments differently depending upon the claims they support. Thus the Eighth Circuit itself deemed the same averments too conclusory to support 1934 Act claims, but sufficient to support 1933 Act claims.

In addition, the courts disagree on the legal effect of a general disclaimer following pervasive averments of fraud. In this case, the court found sufficient to avoid the requirements of Rule 9(b) a general disclaimer that fraud or recklessness was not asserted, even though the plaintiffs had alleged only fraud and reckless-

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[7] The Eighth Circuit acknowledged that its decision was directly in conflict with its sister circuits. (A 7-8.) At least one district court has also held, consistent with the Eighth Circuit, that conclusory fraud allegations under the 1933 Act were not subject to the particularity requirements of Rule 9(b). *In re Consumers Power Co. Sec. Litig.*, 105 F.R.D. 583, 594 (E.D. Mich. 1985). The Sixth Circuit has not yet addressed the issue.

[8] The Eighth Circuit's reliance on this Court's holding in *Leatherman v. Tarrant Co. Narcotics Intelligence and Coordination Unit*, 507 U.S. 163 (1993), as mandating its decision is not consistent with this Court's interpretation of Rule 9(b). (A 8-9.) This Court rejected a heightened pleading standard for civil rights plaintiffs alleging municipal liability not because the cause of action at issue did not require proof of fraud but because the plaintiffs had alleged municipal liability, not fraud. 507 U.S. at 168.

ness, not negligence. The Ninth Circuit has held that such "nominal" efforts to disclaim fraud are insufficient "where the gravamen of the complaint is plainly fraud and no effort is made to show any other basis for the claims levied at the Prospectus." *Stac*, 89 F.3d at 1405 n.2. Accordingly, the Ninth Circuit has applied Rule 9(b) to averments of fraud notwithstanding a plaintiff's purported disclaimer. *Id.* The Eighth Circuit, on the other hand, held that by inserting a one-sentence disclaimer, at the end of 65 paragraphs alleging intentional misconduct, plaintiffs sufficiently "ma[k]e clear that they did not allege in the context of the §11 claim that the defendants were liable for fraudulent or intentional conduct." (A 7.) Under the Eighth Circuit's rationale, a plaintiff is free to damage a defendant's reputation by endlessly repeating the conclusion that the defendant has committed fraud, so long as the plaintiff buries at the end of a lengthy complaint a single line disclaiming all the prior accusations of fraud so as to avoid the reach of Rule 9(b).

The issue presented in this case is likely to recur repeatedly in the future. The Eighth Circuit's decision applies not only to claims under the federal securities laws, but to any case arising under diversity or federal question jurisdiction in which plaintiffs have alleged -- but need not prove -- fraudulent conduct. Moreover, although this case arose prior to the enactment of the Private Securities Litigation Reform Act of 1995, Pub. L.104-67 (the "Reform Act"), the Reform Act did not alter the pleading requirements for claims under the 1933 Act. *Compare* 15 U.S.C. §§78u-4(b)(1) and (2) (1994) (Supp. I 1995) (revising pleading standards for 1934 Act claims) *with* 15 U.S.C. §77z-1 (1994) (Supp. I 1995) (parallel enactment under 1933 Act containing no revised pleading standards). Without action by this Court, this serious conflict regarding the meaning and applicability of Rule 9(b) will continue.

B. The Eighth Circuit's Opinion Abrogates An Entire Category Of Fraud From The Reach Of Rule 9(b).

The Eighth Circuit held that plaintiffs need not comply with Rule 9(b) even if they allege they were misled by statements made without reasonable basis. (A 10-11.) As a result, a significant category of fraud averments is now exempt from Rule 9(b) in the Eighth Circuit. This affects not only securities fraud cases, but every type of fraud under federal or state law if the suit is brought in a federal court.

SEC Rule 175, the safe harbor rule, requires a plaintiff bringing a 1933 Act claim based on a forward-looking statement to plead and prove that the defendant made the statement "without a reasonable basis or . . . other than in good faith." 17 C.F.R. §230.175(a) (1997).[9] Statements made without a reasonable basis have long been recognized as fraud. *See, e.g., Collins v. Burns*, 103 Nev. 394, 397, 741 P.2d 819, 821 (1987) (defining representation made "without a sufficient basis of information" as fraudulent); *Nielsen v. Adams*, 223 Neb. 262, 271, 388 N.W.2d 840, 846 (1986) (holding that defendant is liable for fraud if "a reasonable person in the position of the defendant could not have honestly believed the statement to be true"); PROSSER & KEETON ON TORTS, p. 741-42 (West 1984) (distinguishing between a representation made without sufficient basis, which constitutes scienter or intent to deceive, and mere negligence, which requires an honest belief that the information is true).

Under the Eighth Circuit's ruling, however, this entire category of fraud is no longer within Rule 9(b). Reasoning that a

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[9] The rule provides that "A [forward-looking] statement . . . shall be deemed not to be a fraudulent statement (as defined in paragraph (d) of this section), unless it is shown that such statement was made or reaffirmed without a reasonable basis or was disclosed other than in good faith." 17 C.F.R. §230.175(a) (1997).

statement made without a reasonable basis does not involve "true fraud" within the meaning of Rule 9(b), the court held that "plaintiffs did not have to plead specific facts to avoid the safe-harbor rule." (A 11.) For this entire category of cases, allegations of fraud may now be averred in a conclusory manner, subjecting individuals and companies to the very harm that Rule 9(b) was designed to prevent. This decision dramatically narrows Rule 9(b) and is inconsistent with this Court's purposes in adopting the Rule. This Court needs to provide a uniform rule delineating the scope of Rule 9(b).

II. THE EIGHTH CIRCUIT'S INTERPRETATION OF THE BESPEAKS CAUTION DOCTRINE EVISCERATES THE DOCTRINE AND DIRECTLY CONFLICTS WITH DECISIONS OF OTHER CIRCUITS.

The Eighth Circuit's hostile reading of the bespeaks caution doctrine is inconsistent with this Court's precedent and contrasts sharply with the interpretation of the doctrine by other circuits, including the Third and Ninth Circuits. The judicially created "bespeaks caution" doctrine derives from this Court's definition of "materiality" for purposes of the federal securities laws in *TSC Indus., Inc. v. Northway, Inc.*, 426 U.S. 438 (1976), *Basic, Inc. v. Levinson*, 485 U.S. 224 (1988), and *Virginia Bankshares, Inc. v. Sandberg*, 501 U.S. 1083, 1097 (1991). This Court has held that the materiality of an alleged misstatement must be determined in the context of the "total mix of information" available to investors. *TSC*, 426 U.S. at 449; *Basic*, 485 U.S. at 231-32; *Virginia Bankshares*, 501 U.S. at 1097. If a company predicts a bright future but warns of possible obstacles to success, then the warnings become part of the total mix of information used in determining whether the optimistic prediction is material.

The Third and Ninth Circuits follow *TSC* and hold that whether a risk warning renders a prediction immaterial depends on the "total mix of information," including both prediction and

risk warning. *In re Donald J. Trump Casino Sec. Litig.*, 7 F.3d 357, 369-70 (3d Cir. 1993), *cert. denied*, 510 U.S. 1178 (1994); *In re Worlds of Wonder Sec. Litig.*, 35 F.3d 1407, 1416 (9th Cir. 1994), *cert. denied*, 516 U.S. 909 (1995). These circuits examine the relationship between the prediction and the warning to determine if the warning is sufficiently *tailored* to the prediction to warn investors of the risk that the prediction may not come true. *Worlds of Wonder*, 35 F.3d at 1414 ("cautionary language which directly addresses itself to future projections, estimates or forecasts in a prospectus"); *Trump*, 7 F.3d at 371-72 ("cautionary statements must be substantive and tailored to the specific future projections . . . which the plaintiffs challenge."). If so, the forward-looking statement is adjudged immaterial because a reasonable investor would not consider it significant in light of the total mix of information available. *Worlds of Wonder*, 35 F.3d at 1421; *Trump*, 7 F.3d at 373.

For example, in *Worlds of Wonder*, a company's prediction that it would have sufficient cash to fund its operations for nine months after the offering was held to be immaterial where the company also disclosed its history of operational losses and reliance on borrowed funds. *Worlds of Wonder*, 35 F.3d at 1416. Similarly, the company in *Trump* disclosed its lack of operating history and warned investors that there was no assurance of profit or that operations would meet management's expectations. In light of these disclosures, the Third Circuit held that the company's prediction that operations would generate sufficient cash to repay corporate debts was immaterial. *Trump*, 7 F.3d at 369-70. The Third and Ninth Circuits thus interpreted *TSC* and the bespeaks caution doctrine to require a court to judge the adequacy of risk warnings not in the abstract or in hindsight, but rather in the context of the corresponding prediction. The question is not whether, in hindsight, the warning pinpointed the

timing of future disaster, but whether the warning sufficiently "bespeaks caution" about the prediction.[10]

The Eighth Circuit, through the lens of 20/20 hindsight, ignored the "total mix of information" and instead focused solely on whether the warnings correctly predicted the date of future disaster. (A 13.) The NationsMart Prospectus warned that the company expected to exhaust the offering proceeds of $11.7 million in ten months and that its operations could be expected to yield no profits for at least two years after the offering. (A 12-13.) These warnings were specifically tailored to the company's short-term operational projections, prompting Judge Beam to comment that he could not "envision how or in what manner, defendants could have advanced greater warnings to potential investors so as to avail themselves of the 'bespeaks caution' doctrine." (A 24.) Nevertheless, the court held that the warnings were "generic and non-specific" because they did not adequately warn of a possible cash shortfall in *less than* ten months. (A13.) Thus, considering almost identical predictions and warnings, the Eighth Circuit arrived at the opposite of the conclusion reached by the Third and Ninth Circuits. Indeed, the Eighth Circuit construed the bespeaks caution doctrine in such an attenuated manner that, in effect, it no longer exists in that jurisdiction. As a result, the standard for determining "materiality" in the Eighth Circuit is no longer the "total mix of information" described in *TSC*.

This Court has not yet addressed the bespeaks caution doctrine, and its guidance is now needed to resolve this conflict, to

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[10] Other circuits have also adopted the same interpretation of the bespeaks caution doctrine. *See, e.g., Suna v. Bailey Corp.*, 107 F.3d 64, 70 (1st Cir. 1997) (applying bespeaks caution doctrine because risk warnings were closely related to predictions); *Gasner v. Board of Supervisors*, 103 F.3d 351, 358 (4th Cir. 1996) (holding that "alleged misrepresentations and omissions . . . must be considered in the full context in which they were made," including cautionary language).

elucidate the 22-year-old "total mix" principle of *TSC*, and to provide a uniform rule for determining the materiality of forward-looking statements. The Eighth Circuit's attenuated interpretation of the bespeaks caution doctrine will have a far-reaching effect on corporate vulnerability to strike suits when investors lose money. *See Blue Chip Stamps*, 421 U.S. 723, 740-41 (1975) (noting concern that federal securities laws not become a vehicle to extort large settlements from issuers and insurers). Regardless of where they are headquartered or incorporated, public companies are subject to suit under the federal securities laws wherever their stock is sold, which normally encompasses every federal district in the country, including those of the Eighth Circuit. 15 U.S.C. §77v(a) (1997); 15 U.S.C. §78aa (1997) (broad jurisdiction, venue, and service of process provisions). For this reason, virtually every public company across the country is affected by the Eighth Circuit's decision.

Companies can be expected to respond to that decision by refraining from making any predictions whatsoever. This will disserve investors by depriving them of potentially useful information, the disclosure of which the SEC has encouraged for more than a decade. *See* 17 C.F.R. §229.303(a), Instruction §229.303(b), Instruction §229.10(b) (1997). The threat of strike suits can also be expected to needlessly increase the cost of doing business for all companies, whether they respond by purchasing additional insurance or by self-insuring. These additional costs are wasteful because they add no meaningful information to a "total mix" that already includes adequate risk warnings. The Court's prior decisions have carefully balanced the interests of informing investors and encouraging economic development and entrepreneurship. This Court's guidance is needed to provide a uniform rule in order to maintain that balance.

CONCLUSION

For the foregoing reasons, Petitioners respectfully request that this Court grant a writ of certiorari to the United States Court of Appeals for the Eighth Circuit.

Respectfully submitted,

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